

Detroit Water and Sewerage Department

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Meeting Agenda

Wednesday, February 11, 2015

12:00 pm

Finance Committee Meeting

5th Floor Board Room, Water Board Building

Finance Committee

1. CALL TO ORDER

2. ROLL CALL

3. APPROVAL OF AGENDA

4. APPROVAL OF MINUTES

5. PUBLIC PARTICIPATION

6. OLD BUSINESS

None

7. NEW BUSINESS

A. *Proposed FY 2015 Bondholder Consent Team*

8. REPORTS

None

9. Look Ahead Schedule

Scheduled Meetings

*Finance Committee February 17, 2015, 7:30am Meeting
Annual Finance Committee Report to BOWC- TBD*

10. OTHER MATTERS

11. ADJOURNMENT



City of Detroit
Water & Sewerage Department
Financial Services Group

Date: February 11, 2015

To: Board of Water Commissioners (BOWC) Finance Committee

From: Nicolette Bateson, CPA, Chief Financial Officer

Re: Proposed Financial Services Team to Achieve Bondholder Consent

Proposed Board of Water Commissioners' action item is presented below.

The Board of Water Commissioners for the City of Detroit Water and Sewerage Department authorizes the Director **enter into the following professional services agreements with the firms of Dykema Gossett PLLC (bond counsel), First SouthWest (financial advisor), Citi (underwriter), and The Foster Group LLC (feasibility advisor) to provide the services to seek bondholder consent**, and also authorizes the Director to take such other action as may be necessary to further accomplish the intent of this vote and authorizes the Director to take action as necessary to accomplish this vote.

Agenda of February 11, 2015

Item No. 15- _____

TO: The Honorable Board of Water Commissioners
City of Detroit, Michigan

FROM: Sue F. McCormick, Director
Water and Sewerage Department

RE: Appointment of Dykema Gosset as bond counsel, First SouthWest as financial advisor, Citi as underwriter, and Foster Group LLC as feasibility advisor for 2015 Bondholder Consent Program

MOTION

Upon recommendation of Nicolette Bateson, Chief Financial Officer, the Board of Water Commissioners for the City of Detroit, Water and Sewerage Department authorizes the Director to **enter into the following professional services agreements with the firms of Dykema Gossett PLLC (bond counsel), First SouthWest (financial advisor), Citi (underwriter), and The Foster Group LLC (feasibility advisor) to provide the services to seek bondholder consent**, and also authorizes the Director to take such other action as may be necessary to further accomplish the intent of this vote.

JUSTIFICATION

Professional services are required to achieve 51% bondholder consent as a condition precedent to the execution of a lease between the City of Detroit and the Great Lakes Water Authority for a regional water and sewer system.

BACKGROUND

On September 9, 2014, a Memorandum of Understanding (the “MOU”) was executed to establish the formation of the Great Lakes Water Authority (GLWA). The related Articles of Incorporation were subsequently adopted by the City of Detroit, Wayne, Oakland, and Macomb counties, and the State of Michigan (the “Incorporating Municipalities”). It is intended that the GLWA will assume operation of regional water and sewer services as of July 1, 2015 upon successful completion of a number of conditions. One of those conditions is the consent to the transfer of the water and sewer systems debt to the GLWA from the credit enhancers and a majority (51%) of the holders of City of Detroit Water & Sewerage Department System bonds. A related key condition is the negotiation of a lease between the City and the GLWA by mid-June 2015.

In August 2014, the DWSD initiated a voluntary tender of its bonds. In September 2014, a refunding of the tendered bonds and sale of new bonds resulted in approximately \$1.64 billion of refinancing bonds in addition to approximately \$150 million of newly-issued bonds. The refunded and new bonds provide for bondholder consent to a change in obligor in the event that a regional authority was formed as described in the official statements. That transaction resulted in achieving bondholder consent for approximately 36% of the outstanding water bonds and approximately 33% of the sewer system bonds. To reach 51% consent, the Board of Water Commissioners is tasked with assembling a financial team to explore several paths to achieve bondholder consent.

It is proposed that the Board of Water Commissioners extend the appointment of the 2014 transaction team to carry forward the work begun in 2014 to achieve bondholder consent. The parties have been asked to provide a fee for their services recognizing that achieving bondholder consent can and may be achieved in a number of differing scenarios.

While not a direct comparison, as a benchmark, below is a comparison of the fees if this transaction were \$350 million compare to the combined fees for the \$1.205 billion tender and related subsequent \$1.467 billion refunding and new money transaction.

Advisor	Fee for 2014 Transaction	Fee for 2015 Transaction	Includes expenses?
Financial Advisor (First SouthWest)	\$885,000	\$480,000 (fixed)	No
Bond Counsel (Dykema Gossett PLLC)	\$1,205,000	\$437,500 (based on example transaction size)	No
Underwriter (Citi)	\$2 per bond for Insured Refunding bonds; \$3 per bond for Uninsured bonds; Management Fee: \$1 per bond	No change in per unit fee	No
Feasibility Advisor (The Foster Group LLC)	\$300,000	\$165,000 (fixed)	Yes

The fees proposed are within a reasonable range based upon the 2014 benchmark and the effort that will be required to complete a complex task within a condensed timeline.

It is therefore recommended that the Board of Water Commissioners appoint First Southwest as financial advisor, Dykema Gossett PLLC as bond counsel, Citi as underwriter, and The Foster Group LLC as feasibility advisor. No recommendation is made at this time for pricing consultant to the Board.



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February 2, 2015

Nicolette N. Bateson, CPA
Chief Financial Officer
Detroit Water and Sewerage Department
735 Randolph, Room 1608
Detroit, MI 48226

Via Electronic Mail

Re: Detroit Water and Sewerage Department
Water and Sewage Disposal Systems
Revenue Refunding Bonds, Series 2015

Dear Ms. Bateson:

We are pleased to provide you with follow-up information regarding our interest in continuing to serve as bond counsel to the Detroit Water and Sewerage Department (the "Department") for (i) a limited obligation revenue refunding bond transaction or transactions for savings, together with related matters and (ii) a consent solicitation, structured to solicit and obtain the additional consents necessary under existing bond ordinances to implement the "stand-up" of the Great Lakes Water Authority ("GLWA") as contemplated by the existing Memorandum of Understanding (the "MOU"). This letter is supplemental to our engagement letter of July 14, 2014, which covered the 2014 transactions.

As you know, through the "pivot" which the working group embedded in the bond documents for the Department's 2014 bonds, as long as the GLWA and its master bond ordinances are formally established within the conditions of the "pivot" detailed in 2014, the Department has already effectively obtained investor consents from over 30% of its water and sewer bondholders (51% being the required threshold). In addition, through the Bankruptcy Court mediation process and implementation of the tender transaction in 2014, the Department and its professionals were able to forge positive working relationships with many of the Department's bondholders, its insurers and many of its related stakeholders. We believe this groundwork will serve the Department well as it moves in 2015 towards requesting the necessary consents required by the MOU.

As in 2014, I would expect that fees for our services would be finalized as transactions are finalized in both size and scope. We would expect, however, that for a refunding transaction of approximately \$250 - \$350 million, our bond counsel fee would be approximately \$1.25 per bond, plus customary out of pocket expenses. Similarly, we would expect that our bond counsel fee for the related consent solicitation transactions would be approximately \$1.25 per bond, plus

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Nicolette N. Bateson
February 2, 2015
Page 2

customary out of pocket expenses. This would include traditional bond counsel work, but exclude unrelated work that our firm performs for the Department.

We are delighted to confirm for you our interest in continuing to serve as bond counsel to the Department. We believe that the experience we gained and the relationships with bondholders, insurers and stakeholders we helped you build while implementing the 2014 tender, refunding and new money transactions, will prove invaluable to the Department as it undertakes the next phase of its endeavors. We look forward to discussing this matter with you in greater detail. If you have any questions regarding the matter, please do not hesitate to call me.

Very truly yours,

DYKEMA GOSSETT PLLC



Ann D. Fillingham

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City of Detroit
Water & Sewerage Department
Financial Services Group
February 6, 2015

Proposal from: Citi Public Finance
Thomas H. Green, Managing Director
(Received via email)

Scope

Proposed Dual Track Approach to the Assignment:

Citi proposes a dual track approach to obtaining both the additional consents needed to “pivot” to the GLWA and substantial additional refunding savings.

Consent Solicitation Track. DWSD already has come a long way towards obtaining the necessary majority consents to the pivot as a result of the existing DWSD working group’s successful completion of the August tender and refinancing that closed in early September 2014. As you know, DWSD completed a tender for \$1.72 billion of its bonds and issued refunding bonds, which included specific investor consent for the potential creation of the GLWA and substitution of the “obligor” to GLWA from DWSD. As a result of the 2014 bond issues, investor consent was obtained on more than 30% of each bond credit. Investor consent on more than \$800 million of additional existing bonds is needed to reach the required 51%. For numerous reasons we would welcome the opportunity to discuss in more detail with you and First Southwest, Citi as Consent Solicitation Manager strongly recommends that the remaining consents needed to achieve majority consent to the pivot be sought as early in the 2015 GLWA formation process as possible.

Refunding for Savings Track. Since August 2014, tax-exempt interest rates have continued to decrease substantially. This market improvement has created an opportunity in the current market for DWSD to refund another portion of its outstanding bond portfolio and generate significant additional debt service savings, on top of the quarter of a billion cash flow savings achieved in the initial tender and consent financing. If the current favorable market conditions hold, DWSD issuance of 2015 refunding bonds will provide the BOWC the opportunity to obtain the remaining DWSD bond investor consents that will be needed to effectuate the pivot in the event the definitive agreements are finalized regarding the creation of the GLWA. To take advantage of the current market, Citi recommends DWSD move as quickly into the refunding bond market as the overall process will permit.

Fees

Citi proposes no changes in the fees already agreed to and used in the prior phase of our engagement, except we have added a “credit to DWSD” feature on the Consent Solicitation Manager fee to reflect the fact that there may be circumstances where “Consents to the Pivot” from existing bondholders are obtained from bonds that are then refunded for savings by new bonds with embedded consents at a later phase of the financing process. So, the proposed fees are as follows:

1. Underwriter’s Discount (Quoted as \$ per \$1000 of bond par)
 - a. Sales Takedowns: \$2 per bond for Insured Refunding bonds and \$3 per bond for Uninsured bonds
 - b. Management Fee: \$1 per bond
 - c. Expenses Excluding UW Counsel: usual and customary out-of-pocket expenses only (e.g. CUSIP fee, DalComp, I-Deal, investor and internet roadshow expense and other reasonable and customary out-of-pocket)
 - d. Underwriter’s Counsel and Expense: Citi recommends Debbie Ruskin of Kutak remain UW Counsel and her reasonable and customary fees approved by FSW and DWSD would be an additional expense
2. Consent Solicitation Fee
 - a. \$1 per bond Consent Solicitation with a not-to-exceed cap of \$500,000
 - b. 75% of this fee would be credited back to DSWD against UWD fees for any bonds where consents are initially obtained from existing holders and then the same bonds end up refunded for savings later in the pivot and refunding process

Proposal from: First Southwest Company
Lee Donner, Managing Director
(Received via email)

Scope

First Southwest proposes a dual-track approach, incorporating both (1) current refundings for significant net present value savings, and (2) an organized bondholder consent solicitation, can be implemented in time and with the degree of success necessary to execute a lease agreement between DWSD and GLWA by early June. The financing team that participated in last year's tender/restructuring has the hard earned knowledge and experience to help DWSD's staff execute on what will be a challenging but eminently "doable" undertaking.

Fees

First Southwest propose a fee of \$240,000 for each of the (1) refunding project, and (2) bondholder consent solicitation. In addition, we would ask to be reimbursed for actual out-of-pocket expenses. The primary First Southwest personnel assigned to the project would be myself and Anne Burger Entrekin, but as we hopefully demonstrated across the course of the Series 2014 transaction, we are committed to bringing in additional personnel as necessary to provide whatever expertise is required to advance the project.

TFG
THE FOSTER GROUP

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February 2, 2015

Ms. Nicolette Bateson
Chief Financial Officer
Detroit Water and Sewerage Department
Water Board Building
735 Randolph Street
Detroit, Michigan 48226

Dear Ms. Bateson:

In accordance with your direction, we are pleased to present this proposal to provide business consulting services to the Detroit Water and Sewerage Department (DWSD) related to its upcoming pursuit of bondholder consent related to its currently outstanding Water Supply System and Sewage Disposal System revenue bonds. It is our understanding that DWSD is embarking on a dual track process towards this goal, seeking to acquire bondholder consent through a voluntary process, while at the same time preparing for the potential issuance of revenue refunding bonds for both Systems. It is also our understanding that DWSD will be preparing disclosure documents that are suited to serve either process. Specifically, we have been asked to assist DWSD in this endeavor by providing a feasibility study to be included in the disclosure documents, and to also provide consulting services in preparation of the transactions necessary to acquire bondholder consent. This letter has been prepared to briefly summarize the anticipated work plan and estimated fees to provide such consulting services.

If engaged for this endeavor, we will:

- Conduct all studies we deem necessary to evaluate the feasibility of the proposed transaction, including:
 - An overview of the general DWSD service area, services provided, and operations;
 - An assessment of the general DWSD governance structure, management objectives, strategies, and capabilities;
 - A review of the appropriateness of the proposed capital improvement program;
 - Preparation of a long-term business plan
- Prepare a financial feasibility report summarizing long-term financial projections and our opinions regarding the viability of the proposed transaction;
- Assist the Department in preparing additional disclosure and related support material;

- Participate in all meetings with the core and extended financing teams (and the appropriate working groups) to prepare the financing plan and issuance marketing plan, etc;
- Participate in meetings/presentations with ratings agencies and investors / investor agents;
- Prepare certification analysis regarding compliance with the Additional Bonds Test necessary to issue the Bonds;

Proposed Fees

As we have discussed, the uncertain nature of the pending transaction(s) complicates preparation of a precise estimate of the required level of effort for this engagement. Based on we propose a fee for the consulting services set forth herein is \$165,000. This fee estimate is based on our prior experience in Feasibility Consulting Services for DWSD, and recognizes potential efficiencies of concurrent Water / Sewer transactions. At present, we believe that the estimated level of effort can effectively be equally allocated to the Water and Sewer Systems. To the extent that the transactional delays caused by unanticipated circumstances result in additional efforts, or to the extent that additional analysis is necessitated by such circumstances, we may be compelled to revise this fee proposal.

We sincerely appreciate this opportunity to be of continued service to the Department. If you have any questions regarding this matter, please do not hesitate to contact me.

Very truly yours,

THE FOSTER GROUP



Bart Foster
President